

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
SPENCER GIFTS, INC.	:	DETERMINATION
for Revision of a Determination or for Refund	:	
of Sales and Use Taxes under Articles 28 and 29	:	
of the Tax Law for the Period September 1, 1978	:	
through February 28, 1983.		

Petitioner, Spencer Gifts, Inc., 1050 Black Horse Pike, Atlantic City, New Jersey 08411, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1978 through February 28, 1983 (File No. 800741).

A hearing was held before Brian L. Friedman, Administrative Law Judge, at the offices of the Division of Tax Appeals, Two World Trade Center, New York, New York, on February 2, 1988 at 9:30 A.M. with all briefs to be filed by May 30, 1988. Petitioner appeared by Hutton and Solomon (Stephen L. Solomon, Esq., of counsel). The Audit Division appeared by William F. Collins, Esq. (Lawrence A. Newman, Esq., of counsel).

ISSUE

Whether charges designated by petitioner as "postage and handling" were subject to sales tax.

FINDINGS OF FACT

1. Petitioner, Spencer Gifts, Inc. ("Spencer"), operates a retail sales business. Its mail order division sells gifts through mail order. In recent years, Spencer has mailed out approximately 100 million catalogues and filled approximately eight million orders per year.

2. On July 6, 1983, the Division of Taxation ("Division") issued to Spencer two notices of determination and demands for payment of sales and use taxes due. One notice was for the period September 1, 1978 through February 28, 1982, and it assessed tax due of \$370,106.45 plus penalty and interest. The second notice was for the period March 1, 1982 through February 28, 1983, and it assessed tax due of \$140,845.11 plus penalty and interest.

3. The tax assessments resulted from a test period audit of Spencer's records. As a result of the audit, the Division assessed tax in three areas. Sales tax of \$269,086.60 was assessed based upon the Division's determination of additional unreported sales. Sales tax of \$11,474.38 was assessed based upon Spencer's failure to pay tax due on its own purchases of taxable fixed assets. Finally, the Division assessed sales tax of \$230,390.58 based upon its determination that charges called "postage and handling" on Spencer's mail order forms were subject to sales tax.

4. Following a Tax Appeals Bureau conference, the Division agreed to reduce to \$71,639.57 that portion of the assessment based upon additional unreported sales. Spencer

conceded tax due of \$11,474.38 on its purchase of fixed assets. The Division agreed to abate penalties above the minimum on the entire assessment. Petitioner executed a withdrawal of petition as to those items agreed to by the parties; therefore, the only area before the Division of Tax Appeals is the Division's imposition of sales tax on charges denominated "postage and handling".

5. During the audit period, Spencer used a mail order form on which the customer calculated a charge for postage and handling. The customer was instructed to calculate this charge by referring to a postage chart. The chart declared: "Avoid delay by including postage and handling charges with orders. These small charges represent only part of total costs. We pay the rest."

6. The amount charged by Spencer for postage and handling was based upon the total purchase price of an order. In October 1978, customers were charged 85 cents for orders up to \$3.00, \$1.15 for orders from \$3.01 to \$5.00, etc. The maximum charge was \$2.85.

7. The audit at issue consisted of a test of orders received by Spencer during a three-day period in July 1981. In those three days, Spencer received approximately 10,000 orders, of which 472 orders were from New York residents. The auditor prepared a listing of the New York orders, showing that each order contained a separately stated charge for postage and handling. The charges were no less than 95 cents nor more than \$3.15. The Division did not perform independent analyses to identify those tasks which might be included under the term "handling" or to determine the relationship between the amounts charged for postage and handling and the costs incurred by Spencer in mailing or shipping orders.

8. The amounts Spencer charged its customers for postage and handling were established by its marketing division based on the prevailing rates charged in the mail order industry. The charges were imposed to enable Spencer to recover its own costs in transporting merchandise from its warehouses to the customer.

9. Spencer shipped its merchandise to its customers by United Parcel Service or United States mail. In both cases, the charge to Spencer was determined by the distance shipped and the weight and size of the package shipped. In a particular case, the amount Spencer charged for postage and handling might be more or less than the actual cost to Spencer of shipping a particular package. In the aggregate, amounts Spencer received for postage and handling did not cover the cost to Spencer of shipping by United States mail or private carrier.

10. The Division performed no analysis to determine whether Spencer's charges for postage and handling were reasonable, and it took no position on this issue.

11. Spencer has been in the mail order business since 1947. It used the term "postage and handling" on its mail order form from that time until sometime in 1986. After the audit at issue, Spencer revised its order form by replacing the term "postage and handling" with the term "transportation costs".

SUMMARY OF THE PARTIES' POSITIONS

12. It is the Division's position that the term "postage and handling", as used by petitioner, denoted two separate charges: one for postage and one for handling. It concedes that a charge for postage would be considered a transportation cost and thus excluded from the operation of the Sales Tax Law. It deems handling charges to be taxable. As petitioner included postage and

handling together as one charge, the Division deems the whole amount to be taxable.

13. The Division points to the fact that the postage and handling charge was calculated on the basis of the total cost of merchandise shipped as evidence that the charge was not solely for transportation. It is the Division's position that, to qualify as a transportation cost, each individual charge for postage and handling must have been identical to the amount Spencer was charged by its carrier (the United States Postal Service or United Parcel Service) for the delivery of that particular order.

14. Spencer contends that the term "postage and handling" is a common idiom used in the mail order business to denote costs for the transportation of goods to the customer. It also argues that, regardless of the nomenclature used, its postage and handling charge qualified as a transportation cost pursuant to the Rules and Regulations of the Commissioner of Taxation.

15. Neither the Division nor Spencer attempted to categorize those tasks which would be includable as handling charges as opposed to transportation costs. Spencer argued that even if some portion of its postage and handling charge was for handling, the Division would be required to allocate the amount attributable to the taxable charge and exclude the balance from tax. As Spencer's overall costs for mailing and shipping were more than its total charges for postage and handling, it argued that no part of the charge could be attributed to handling.

16. Spencer maintains that the Division's failure to raise any issue regarding postage and handling charges on prior audits of Spencer creates a presumption that those charges are not subject to sales tax.

CONCLUSIONS OF LAW

A. Tax Law § 1105(a) imposes a tax upon "receipts from every retail sale of tangible personal property". Excluded from the definition of "receipt" is "the cost of transportation of tangible personal property sold at retail where such cost is separately stated in the written contract, if any, and on the bill rendered to the purchaser" (Tax Law § 1101[b][3]). The Rules and Regulations of the Commissioner of Taxation and Finance set forth three criteria which must be met to qualify a charge as a transportation cost under Tax Law § 1101(b)(3). The transportation cost "must be for the delivery of the tangible personal property to the purchaser" (20 NYCRR 526.5[g][2]); the charge must be separately stated, meaning that it can be computed from information appearing on the bill (20 NYCRR 526.5[g][3]); and the "charges must be reasonable in relation to prevailing established rates" (20 NYCRR 526.5[g][4]).

B. The primary question to be determined is whether the charge denominated by petitioner as "postage and handling" was a charge for delivery of merchandise, excluded from the definition of a receipt, or whether it was an incidental charge properly included within the definition of a receipt.

Petitioner presented uncontroverted testimony at hearing that the term "postage and handling", as used on its mail order form, denoted a charge for delivery of merchandise from petitioner's warehouse to the purchaser. In the case of an individual order, the charge for postage and handling might be more or less than the actual cost to petitioner of mailing or shipping; however, in the aggregate, amounts collected by petitioner for postage and handling were less than its overall postage and shipping costs. Petitioner maintains that those facts established that its entire postage and handling charge was for delivery of merchandise and that none of the charge was for handling. It contrasts its own billing practices with that of the petitioner in

Matter of Lillian Vernon Corporation (State Tax Commission, October 22, 1982). There the Commission found that 40 percent of petitioner's charges for postage and handling constituted handling charges; therefore, the entire charge was found subject to sales tax.

The Division relies on the fact that petitioner's postage and handling charge was not identical to the amount petitioner was charged for mailing and shipping by its own carriers as proof that the postage and handling charge was an incidental charge for a service other than delivery of the merchandise. Its rationale is predicated upon its general position that the term "cost of transportation" as used in Tax Law § 1101(b)(3) is confined to the actual costs of postage, shipping and freight charges, in each individual case (see, e.g., Sales Tax Newsletter, Volume 12, No. 2). As applied to this petitioner, its argument is not persuasive.

Neither the statute nor the regulations explicitly confine transportation costs to the actual costs of postage, shipping and freight charges. The regulation merely requires that "charges be reasonable in relation to prevailing established rates" (20 NYCRR 526.5[g][4]). Proof that petitioner's rate schedule was established solely by reference to the prevailing rates charged by competing mail order houses was adequate to show that its charges were reasonable in relation to prevailing established rates. As there was uncontroverted evidence that no portion of petitioner's charge was attributable to handling or any other service (compare, Matter of Lillian Vernon, supra), it is concluded that the entire postage and handling charge was for delivery of merchandise from petitioner's warehouse to its customer.

C. Petitioner has established that, regardless of the nomenclature employed, its charge for postage and handling qualifies as a transportation cost on the basis of the three criteria set forth at 20 NYCRR 526.5(g)(2), (3), and (4). Accordingly, its charges for postage and handling are excluded from the definition of a receipt found at Tax Law § 1101(b)(3). The Division is directed to cancel that portion of the assessment, totaling \$230,390.58, based upon the postage and handling charges.

D. In accordance with agreements reached by the Division and petitioner, petitioner's tax liability has been reduced to \$83,113.95 plus minimum interest (see ___ Finding of Fact "4").

E. The petition of Spencer Gifts, Inc. is granted to the extent indicated in Conclusions of Law "C" and "D"; the notices of determination and demands for payment of sales and use taxes due issued on July 6, 1983 shall be modified accordingly; and in all other respects, the petition is denied.

DATED: Albany, New York
September 15, 1988

/s/ Brian L. Friedman
ADMINISTRATIVE LAW JUDGE